House Policy Committee

Policy Perspective

Christopher Cox, Chairman

<u>Congress Repeals Death Tax</u>

Funeral for the Death Tax

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On August 5, Congress passed the Financial Freedom Act of 1999. One key provision of this historic tax reform legislation will phase out the Federal tax on estates and gifts, commonly known as the "Death Tax." The tax reform bill just passed by Congress will gradually reduce the Death Tax, repealing it completely in ten years.

This historic reform builds on important Death Tax relief enacted as part of the Taxpayer Relief Act of 1997, which provides for a phased increase in the amount exempt from the tax through 2006.

Repeal of the Death Tax is a bipartisan effort: Although President Clinton has adamantly opposed Death Tax reform, his own White House Conference on Small Business has made repeal of the Death Tax a top legislative priority. California voters repealed their state's Death Tax by almost a two-to-one margin in a 1982 referendum; since 1997, five states (Delaware, Iowa, Kansas, Louisiana, and New York) have repealed or significantly cut their Death Tax burdens.

The reason is for this bipartisan, nationwide support is clear: the Death Tax violates all the basic principles of a good tax system. It is complicated, unfair, and inefficient. Indeed, a recent report by Congress' Joint Economic Committee concluded that the Death Tax "has no redeeming qualities." According to the report, the Death Tax results in "slower economic growth, reduced social mobility and wasted productive activity." The report found that "the costs imposed by the [Death Tax] far outweigh any benefits that the tax might produce."

The Joint Economic Committee also found:

- The Death Tax in this century has reduced the stock of capital in the economy by almost half a trillion dollars, some 3.2 percent.

2471 Rayburn House Office Building (202) 225-6168 FAX (202) 225-0931
E-mail: policy@mail.house.gov http://policy.house.gov

- The Death Tax causes inefficient allocation of resources, discouraging saving and investment and lowering the after-tax return on investments.

- Death Tax rates are extremely punitive, with marginal rates from 37 percent to nearly 80 percent on an individual's after-tax life savings, including life insurance.

- The Death Tax is a leading cause of dissolution for thousands of family-run businesses. Death Tax planning further diverts resources available for investment and employment.

- Empirical and theoretical research indicates that the Death Tax not only fails to reduce inequality of wealth, but may actually increase concentration of wealth by forcing the sale of small businesses, farms, and land holdings to larger companies.

- By contrast, the truly wealthy can largely avoid paying the Death Tax: wealthy taxpayers who can afford to pay the necessary legal fees and life insurance premiums, and who can restructure assets in a manner that does not build their businesses, will not bear the brunt of the Death Tax.

- Those most affected by this tax are those who have built small businesses and those who own and work on family farms. The burden of this tax falls on entrepreneurial small businessmen and women, and on the workers who lose their jobs when a family business, ranch, or farm is liquidated to pay the Death Tax.

- The Death Tax obstructs environmental conservation. Large Death Tax bills often force families to sell or develop environmentally sensitive land.

- The Death Tax raises very little, if any, net revenue for the federal government. Enormous compliance costs associated with the Death Tax are of the same general magnitude as its revenue yield, or about $23 billion in 1998 according to the Joint Economic Committee. Even ignoring compliance costs, the tax raises barely one percent of federal receipts.

Most people are familiar with the concept of a "sin tax"—a government levy on goods or behavior deemed damaging to society or individuals, such as cigarettes and alcohol. The Death Tax is the opposite of a sin tax -- it is a virtue tax. The Death Tax penalizes the very behavior that is considered virtuous and should be encouraged: savings, investment, and most importantly, work. Its bias against savings is matched only by its bias in favor of immediate consumption. It impedes the upward mobility of labor by stifling productivity, wage growth, and employment opportunities.

By passing historic tax reform legislation repealing the Death Tax, Congress has struck a blow for families, workers, farmers, and small businesses throughout America.

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